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Highlights: NPCI's Standard Operating Procedure for the UPI TPAP Volume Cap

On March 25, 2021, the National Payments Corporation of India **("NPCI")** released the long awaited Standard Operating Procedure ("**SOP**") for implementation of the 30% volume/market share cap on the Unified Payments Interface **("UPI")** platform. These SOPs would apply to all Third-Party Application Providers ("**TPAPs**") operating on the UPI platform.

Background

The NPCI had through a circular dated November 05, 2020 ("**Volume Cap Circular**") imposed a condition on TPAPs to ensure that the total volume of transactions initiated through a TPAP's UPI application does not exceed 30% of the total volume of transactions processed in the UPI system ("**Cap**"). The Volume Cap Circular clarified that transaction volumes would be calculated on the basis of transactions processed in UPI during the preceding 3 months on a rolling basis. The Volume Cap Circular came into effect from January 01, 2021, but existing TPAPs were given until December 31, 2022 to comply, in case their transaction volumes exceeded the Cap as on December 31, 2020.

Features of the SOP

Notably, the design principle of the SOP is to implement the Cap by controlling user on-boarding on a TPAPs' UPI application. As per the SOP, the NPCI expects the market share for TPAPs to reduce naturally, once new customer on-boarding is moderated. The SOP defines 'moderated on-boarding' as the process of allowing only up to 50% of total customer on-boarding requests. If such measures do not result in a reduction in market share, the NPCI will discuss modalities with non-compliant TPAPs – including a restriction of new customer on-boarding altogether. The SOP clarifies that the NPCI intends to implement the Cap with as little inconvenience to users as possible, by ensuring that transactions initiated by existing users are not declined, as far as possible.

We have summarised below in brief the key provisions of the SOP:

1. **Calculation of market share of TPAPs**: The SOP provides for the following formula to calculate the market share of a TPAP:

   Market Share of TPAP (%) = (TPAP UPI Transactions)/(Total Volume of UPI Transactions)

   For the purpose of the formula:

   i. '**Total Volume of UPI Transactions**' means the aggregate of all successful financial transactions in UPI ecosystem. Payments to UPI IDs, account number + IFSC combinations, mandate transactions and other future account types that will be implemented will be considered in the calculation. This includes P2P, P2PM and P2M transactions through various modes, such as Push, Collect, Intent, QR and any other future modes including B2B and B2C transactions.

   ii. '**TPAP UPI Transactions**' includes <u>all of the above transactions</u>, initiated through a TPAP's UPI application, with the exception of pre-approved B2C and B2B transactions. Pre-approved B2C and B2B transactions are credit transactions in the nature of merchant or customer cashbacks, rewards, merchant settlements, corporate disbursements, vendor payments, refunds and any financial incentives provided by TPAPs to their users.

   The Cap is applicable only for the transactions initiated from a TPAP UPI application acting a 'payer' and will not be applicable for the recipient end, i.e., payee TPAP end. Further, the SOP also clarifies that 'on-us' transactions, i.e. transactions that are not processed and settled through the UPI central system, must be reported by TPAPs on a monthly basis to the NPCI, and will also be included in 'Total Volume of UPI Transactions'.

2. **Monitoring of UPI transactions threshold**: In order to ensure that TPAPs comply with the Cap, NPCI will monitor TPAPs market share, and will send alerts upon a TPAP breaching three thresholds:

   i. **Level 1:** Upon the market share of a TPAP breaching 25%, an alert will be sent to the TPAP and its payment service provider banks ("**PSP Banks**") by way of email/letter. On receipt of the communication, both the PSP Banks and TPAP are required to acknowledge the alert.

   ii. **Level 2:** Upon the market share of a TPAP breaching 27.1%, a second alert will be sent to the TPAP and its PSP Banks. TPAPs and PSP Banks will be required to provide evidence of actions taken to comply with the Cap.

   iii. **Level 3:** Upon the market share of a TPAP breaching the Cap of 30%, the TPAP and its PSP Banks must stop on-boarding new customers and provide an undertaking that they will achieve compliance.

3. **Temporary Exemption:** Upon breach of the thresholds, **t**he NPCI, upon request by PSP Banks, may exempt their TPAPs to certain extent when the Cap is reached, after evaluating the case basis the (i) justification provided; (ii) recommendations from the PSP Banks; and (iii) after studying the impact on the UPI ecosystem. While the exemption will last up to a maximum period of 6 months, it may be extended at the discretion of the NPCI. Further, as per the SOP, during the period of exemption, if the market share of a TPAP is nearing or has breached the Cap, the TPAP may be asked to immediately moderate the on-boarding of new customers and come up with an action plan to remedy the non-compliance. If it is observed that the TPAP continues to on-board new customers without moderation, the NPCI will issue a notice to stop on-boarding.

4. **Reporting:** The NPCI has been reporting UPI applications' transaction volumes and values on its website. As per the SOP, the NPCI will also improve the manner of reporting to be in accordance with the SOP. Further, the NPCI will also share details of TPAP volumes, compliance with the SOP, and actions taken, with the regulator.
5. **Penalty:** If a TPAP is not compliant with the Cap or such breach is not remedied during the exemption period, the NPCI may levy a penalty on the TPAP in accordance with the UPI Procedural Guidelines. It may also block new user on-boarding, by the TPAP, from its central UPI system.

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